WORLD JURIST ASSOCIATION'S

CONFERENCE ON INTERNATIONAL TERRORISM

MADRID, SPAIN ; APRIL 14 - 17, 2002

SPECIFIC PERIL TERRORISM COVER --

A PROPOSED PARTNERSHIP OF INSURANCE ESTABLISHMENTS AND GOVERNMENTS WORLDWIDE

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I. INTRODUCTION.

The consequences of September 11th continue to unfold and all but numb the mind. It is still difficult to comprehend the enormity of the event and its impact on men, women and children of every faith, its dislocation of economic institutions, and its rewriting of governmental policies worldwide. Efforts to recompense, repair, and rebuild, as well as to protect against future terrorist acts, dominate the agendas of our personal, business and governmental communities. Terrorist's ultimately seek the destruction of the individual's belief in personal security, trust in government and freedom from fear. The ultimate mission of the insurance establishment is the strengthening of an individual's sense of security, trust and courage when facing significant losses or personal danger. Achieving this goal directly attacks the terrorists' most valued weapon - - fear. Thus, the insurance community in each developed nation has a unique opportunity to continue to play and to expand its significant societal role to directly fight this old but newly dangerous enemy. Yet the magnitude of potential terrorist losses presents a threat to their solvency such that the insurance establishment cannot continue, let alone expand this coverage component alone.

Historically, insurance has protected both businesses and individuals from catastrophic losses arising from most all risks, except notably a declared war. This paper proposes a partnership between the insurance establishment in each developed nation and its government that would effectively pair the infrastructures, unique resources and capital of these entities in order to unhesitatingly respond to future terrorist-caused losses ("Program"). Insurance establishments worldwide would not be called upon to assume more risk than they could underwrite in order to create this Program. Indeed, if governments will underwrite the risks of terrorism in partnership with them, in a manner that permits classic market forces to establish the line between private sector and government coverage, insurers can seize this opportunity to fulfill their ultimate mission without risking insolvency. This Program would not require

dramatic changes to the infrastructures of either the insurance market or the government of each nation participating in the Program, nor in the laws that govern both of them. Moreover, the creation of this Program need not be delayed until resolution of the myriad of general civil justice and public policy issues that dominated insurance, tort and government reform agendas before September 11th. As societies resolve these far reaching questions, the resulting solutions can simply be applied to this Program as well.

The Program would establish a considered and soundly structured Specific Peril Terrorism Cover. Reliance on "all risk" covers for future loss from terrorist attacks would not provide the certainty now needed for the assumption of this risk. All claim handling functions would remain the responsibility of the participating carriers. Once the losses from one given terrorist event, a series of such events, or a number of separate events exhaust fairly determined and specific "sub-limits" for these specific perils provided by an individual insurance company, its government would "back-stop" it by paying the remaining loss up to a similarly determined nation-based specific peril "limit." When an individual nation could not pay such a loss with the combined specified resources of its treasury and the relevant insurance, an international fund, created by nations choosing to partner one with the other, would serve as the "insurer of last resort". This fund would most effectively be created under the auspices of the United Nations, in whatever manner or charter was acceptable to participating nations (the "U. N. Fund").

The Program's three progressive tiers of coverage -- insurance sector, government sector and U. N. Fund -- would be financed by premium at the private layer, with governmental revenues and treasury surpluses being used at the national and international layers. Thus, a carrier, whose loss on a given claim reached either the government or the U. N. Fund limits (attachment points), would continue to administer that claim, but the monies necessary to pay the loss above its per event or aggregate limits would come first from its government and thereafter, if needed, from the U. N.

Fund. Defense of disputed claims, however, would be funded only at the individual carrier level.[1]

The insurance establishments in each developed nation can continue to provide protection from the consequences of terrorist acts. If insurers are to succeed in this mission, there must be changes made to permit classic coverage lines to continue to stay solvent. These lines include: (1) life, workers' compensation, health and accidental benefits ("Personal Lines"); (2) first party protection against fire and other forms of destruction ("Property Lines"); and (3) third party protection for casualty claims and lawsuits ("Casualty Lines"). The Program contemplates utilizing these Lines of cover and traditional market theories, insurance principles, and the "rule of large numbers" to keep solvent a voluntary partnership, on a national and worldwide scale, that can spread the risks and allocate the losses of terrorist events more effectively and safely than could either partner alone. As for those undeveloped nations that do not have insurance establishments, but seek the protection of such an economic asset, carriers worldwide would have an opportunity to help create "new markets" in those sovereign states. A Specific Peril Terrorism Cover ("SPTC") Program could thus ensure, in significant part, a global response to what is a global problem.

II SEPTEMBER 11TH ALTERED THE FUTURE COURSE OF INSURANCE ESTABLISHMENTS, BUSINESS COMMUNITIES AND GOVERNMENTS WORLDWIDE.

A. The Impact on the Insurance Establishment.

The attack of September 11th took the lives of nearly 3,000 peoples, devastated four to five times that number of other lives, and resulted in catastrophic commercial losses. Most analysts currently estimate that quantified in terms of dollars, as opposed to the very real misery, suffering and harm that it is at the core of this event, this single loss will eventually amount to well over $50 billion.

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[1] At the beginning of the Program, the governmental and U. N. Fund cover might also have to serve as a re-insurance backstop while certain disputes and issues, detailed below, relevant to this cover are resolved.

Property, Casualty and Personal Lines will cover a significant amount of that loss. The Property/Casualty Lines are not invoking act of war exclusions (Personal Lines never did and do not, as yet, have such limitations). Across all of these Lines, the carriers tried to do what insurance companies have historically done -- to protect, to make secure, and to help turn fear, anger and loss into resolve and hope. Direct insurers, those who actually handle the claims and deal with claimants and policyholders, will pay about one-third of the total loss, while re-insurers will pay two-thirds.[2] However, some re-insurers are threatening to dispute coverage based on war risk exclusions.

September 11th losses are being paid by various specific types of insurance as follows: (1) workers' compensation carriers will cover approximately $5 billion in losses; (2) life carriers will cover approximately $6 billion; (3) Property Lines will pay about $12 billion; and (4) Casualty Lines will pay between $18 and 20 billion. Target defendants for third party casualty claims include building owners, airlines, and local, state, and national government agencies that provided protection and rescue services. Many of the carriers responding to September 11th are domestic.. However, of that loss, 60% will be covered by carriers with principle places of business outside of the United States.

In a companion paper from this panel, James L. Seal of Berkes Crane Robinson & Seal, LLP in Los Angeles, California, discusses the availability of insurance coverage for terrorist-related losses under policies which currently exist and the inadequacy of policy provisions as presently drafted to focus on the types of terrorist-related risks which insurers may now wish to limit or exclude. Traditionally, life insurance, workers' compensation insurance and first party (at least fire coverage)

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[2] Re-insurers "cover" direct insurers by repaying them a significant portion (generally 60 to 80%) of their indemnity losses under either an individual policy (facilitative cover) or group of policies (treaty cover). Re-insurers are themselves covered by retrosessionairs. Retrosessionairs lay off some of their risk to yet other insurance groups. Generally post-direct market carriers charge their "insureds" a percentage of the premium collected by the latter from their policyholders for this cover.

insurance does and must respond to any act of terrorism. Even acts of nuclear, chemical or biological terrorism are not excluded from most Personal Lines. This is because these are traditionally "all risk" as opposed to "specific peril" covers. Likewise, Casualty Lines generally use "all risk" forms (except for E&O, D&O, and Personal Injury covers) and a carrier is liable for terrorist losses unless they fall within the definition of a war risk or other applicable exclusion or condition.[3] In the United States insurance companies are regulated in each state, the District of Columbia and Puerto Rico (the "52 jurisdictions"), rather than on a national of federal basis. Therefore, there are some anomalies in the foregoing, but not in the industrial states or the major centers of commerce.

To put the impact of the $50 billion loss of September 11th into perspective, the Pan Am jet that exploded over Lockerbie, Scotland in December 1988 killed 270 people and resulted in an insured loss of approximately $138 million. The destruction of the Federal Building in Oklahoma City in April 1995 killed 168 people, injured 487 more and resulted in an insured loss of $145 million. Hurricane Andrew resulted in $19-22 billion in insured losses in 1992. It is estimated that Andrew's losses equaled 6.3% of the total 1992 U.S. insurance surplus for *all* Lines. Assuming a current U. S. insurance surplus of $300 billion, the consensus loss of $50 billion would equal over 16% of that amount. Note, however, that the Property and Casualty Lines that cover 60% of the total loss ($30 billion) account for only one-third of that surplus ($100 billion). Their specific losses are equal to 30% of that *segregated* portion of the surplus. To further put that percentage in context, there is about $125 billion in current re-insurance surplus. At the end of the day, the direct Property/Casualty market *and* its re-insurers lost only 13% of their combined surplus. This puts into graphic relief the impact on direct insurers of any loss of re-insurance cover for this risk.

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[3] See the discussion on the currently proposed ISO terrorism exclusion for Property/Casualty Lines in Part II. B., below.

It is beyond debate that several more significant terrorist acts, or even one more event with losses greater than those on September 11th, will present a demand on the insurance establishment in general and on individual carriers in particular that risks significant insolvencies across the market. While the direct primary, umbrella and excess carriers in all Lines responded admirably to September 11th losses, they have had to take stock of future risk options in light of their combined $300 billion surplus. A number of government and private entities in the U. S. directly and indirectly analyze and govern the conduct of the insurance establishment. Separate regulatory agencies operate in all 52 non-federal jurisdictions in the U. S. These agencies, together with the National Association of Insurance Commissioners (NAIC), private sector rating and creditworthiness services, bank analysts and insurance professionals, all serve as insurance establishment "watch dogs." The foregoing entities have been monitoring the direct insurance carriers' ability to withstand the present and future losses, while at the same time analyzing the coverage limits available in this market, the re-insurance market and the retrosessionairs market. The consensus judgment is that few carriers can stay solvent, let alone have sufficient cash, if called upon to respond fully but alone to all future terrorist caused losses. Market pressures already at play have served to put some companies on a negative rating watch or on a credit watch because of their September 11th payments and future like risks.

One of the key factors in the current solvency debate is the refusal of many re-insurers to "follow the fortunes" of their policyholders (the direct insurance market). Many re-insurers are invoking or adding war or terrorism exclusions to their treaties and facilitative contracts. The direct market has not invoked these bars to coverage and their "fortunes" include paying claims the re-insures have now disputed. As re-insurance claims have found their way though the traditional processes and as renewals of re-insurance have come up for negotiation, the "exclusion" debate has brought added instability to the operation of insurance markets worldwide. All of these circumstances have led to attempts to exclude terrorism from coverage in the direct

market until the risk can be comprehended, undertaken and re-insured (See Part II. B., below).

Moreover, general insurance premiums are increasing significantly to cover current and future terrorist losses. There is not now, and probably will not be, separate terrorism cover pricing that can succeed in the general, as opposed to specialty markets. That process is already underway in all cover Lines. These increases are occurring in the context of a "stiffening" premium market, that began about a year before September 11th and which served to increase pricing for the first time in over 10 years. I*n the absence* of any terrorist exclusions, since September 11th premiums have increased anywhere from 10% to 20% to up to 200%, depending on the Line and the perceived terrorist risk. The few carriers who are today continuing to offer terrorism cover without recourse to newly offered exclusions or limitations (See Part II. B., below), can only do so in specialty markets. Thus, to the extent that coverage is being offered, it is often available to only to a few who have discrete terrorism risks and great financial resources.

At the same time the direct market is attempting to recover in its complex and diversified regulatory context, the re-insurance market is free from those constraints and has signaled that it will, in large measure, apply terrorism exclusions to all of its new policies and/or involve war risk exclusions. Without re-insurance, the direct market has to exclude the risk, obtain premium enough to protect solvency, or "go bare." Classic market dynamics control this issue. Yet, as the parties seek to work their way through this impasse, there appears to be no agreed solution to this problem for the immediate or foreseeable future without government intervention.

As noted above, there are segments of the market that are not facing the "exclusion question" just yet. Depending on the capacities of the insurer, the position of its re-insurer and a potential to specifically limit the risk either by "geography" or line of business, some terrorism cover is still available at market driven premiums (as

high as 200% more than before September 11th). Where the coverage is made available, carriers are increasing deductibles and lowering limits for this risk. The risk has increased, premiums are going up, the availability of re-insurance is unclear, and new as well as continued coverage is at risk.

B. The Insurance Establishment Considers Limits to and Exclusions for Terrorism Cover.

The Insurance Services Offices ("ISO") is an independent entity that, nevertheless, can act on behalf of Property and Casualty insurers to suggest a comprehensive approach to the terrorist risk issues raised for Property and Casualty Lines. ISO is the entity that proposes premium rate structures and standard policy provisions on behalf of insurers in each of the 52 jurisdictions. Over the past several months, ISO drafted and presented a terrorism coverage limitation/exclusion for Property and Casualty policies to each of the 52 jurisdictions. Currently, all but five jurisdictions have accepted the proposed exclusion as *an interim measure*. In the remaining five, the relevant regulatory agencies have either denied approval of the exclusion or suggested revisions and language pending approval.

The stated reason for presenting and adopting the ISO exclusion was to protect insurer solvency while the current debate over the future of this cover plays out. In any given year, the Property and Casualty insurers in the U.S. collect approximately $300-$400 billion in premiums. As noted above the Property/Casualty surplus in the U. S. is about $100 billion of a total $300 billion for all Lines. Yet, the total possible loss they protect has been estimated to amount to over $5 trillion in replacement value and another $5 trillion in inventory, equipment and software on the Property side, not to mention the untold value of the lives of more than 250 million people.

The exclusion actually serves to limit as well as to exclude coverage that each individual company must now, by law, provide, even without the protection of re-insurance. Under ISO's theory, carriers could offer a limited level of coverage, as

provided for in the ISO exclusion, even without re-insurance or until such time as that issue is solved. There is a debate as to whether exclusion approvals should contain a "sunset clause" that revokes this provision should government "back-stop" coverage become available. The U. S. Government could simply "back-stop" private sector coverage by assuming that part of the loss that would otherwise risk insolvencies in the market. At this juncture, only California, Florida, Georgia, New York and Texas have not finalized their response to the exclusion. However, these states account for 35% or more of the total product of the current U. S. insurance market.

Under the ISO exclusion, if a given terrorist attack (however that is ultimately defined) results in an aggregate loss of $25 million *or less*, Property and Casualty policies will cover the damages. If a given loss *exceeds* $25 million, there will be no coverage, not even the for the first $25 million. There are specific rules that govern calculation of the $25 million limit that rely upon various time, geographic area and loss definitions. Every terrorist loss covered in current "all risk" policies that adopt this exclusion contributes to the $25 million limit[4]. The exclusion defines multiple acts that are coordinated or carried out "in concert" as one event. The $25 million cap applies to one event. Splitting one event into two or more acts would permit multiple $25 million "payments." There is currently a dispute as to whether September 11th was a one, two or multiple-event loss; i.e., should separate limits apply to the combined losses flowing from each attacked building and to the plane lost in Philadelphia, or was this did all loss simply flow from one concerted act/event?

There is an alternative limitation in the exclusion that provides that if a terrorist event causes death or serious physical injury to 50 or fewer persons, the policies will cover those losses. However, *if more than* 50 persons are involved, there is no cover, not even for the first 50 claimants. This is true even if total damage are

[4] All risk Property/Casualty policies are currently subjected to exclusions for war and nuclear, biological or chemical losses caused by terrorism. The ISO exclusion does not add back cover for these exclusions.

$25 million or less. The breadth of the ISO exclusion's definition of a terrorist act and its provision for either up to only a $25 million/50 person loss *or no coverage at all* are still the subject of much debate. As yet un-addressed is the question of such an exclusion being added to Personal Lines.

It is clear that there has to be some protection for insurance companies while this risk is assessed and the current disputes between the direct and re-insurance markets continue. Nevertheless, even at a $25 million or less level, if one entire loss is borne by a single insurer, it could still threaten its solvency, (depending on its premium bases and surplus). In the absence of re-insurance, approximately 44% of the Property /Casualty insurance companies in the United States could very well have serious financial difficulty handling a single $25 million loss. The obvious solution to this dilemma is to permit each company to customize its terrorism cover limit exposure based on its own surplus and premium base. However, given the current 52 U. S. regulatory jurisdictions, such customizing is difficult and time consuming to present and approvals would probably be slower still. Moreover, there would be insufficient cover under the ISO plan for most of the insureds that realistically face this threat. Meanwhile, a carrier has the choice of continuing to write this cover and living with its increased exposure or of withdrawing from the market. Neither of those solutions is acceptable, let alone attractive. Neither of those solutions advances the goal of preserving a market driven insurance program to protect against the risk of this specific peril.

C. The Impact on the Business Community.

All commercial property owners and businesses are facing higher premiums, even though in many cases their policies soon will reduce or exclude terrorism coverage. The loss or restriction of this coverage has a direct and adverse impact on the nation's economy. For example, owners of large groups of buildings in major metropolitan centers can have a total risk of $100 million to $1 billion. Prior to September 11th, a loss caused by terrorism would be covered under various Lines of

coverage held by these owners. Today, those owners could, in large part, only obtain $25 million of coverage, if it is even to be available under the ISO exclusion. Those who can obtain this coverage can do so only at increasingly high market driven premium rates. Otherwise, these owners must "go bare."

To the extent that banks still are backing loans on business and properties, they cannot obtain the previously guaranteed levels of insurance. Are banks to call their loans or, like the building owner, "go bare?" Suppose the tenants in the building are asked to absorb the premium increase. Can building owners simply pay 10%, 20%, 30% or up to 200% more than they did in the past and pass that cost on to tenants? Individuals or entities that buy shares in building loan programs have the same hard choices to make. Thus real estate and commercial lending entities are experiencing significant problems in protecting their existing properties and those difficulties are magnified tenfold for purchase or sale of real estate, for financing of businesses and for construction of large new projects.

The players in the commercial and business communities are understandably concerned. They do not have the ability to allocate their risk or spread their loss on the scale that insurance companies can provide. Another terrorist attack raises the specter of bankruptcies, forced sales, loan defaults, and other losses. The business and commercial communities have, therefore, lobbied hard for a governmental "back-stop" of terrorism insurance and re-insurance under a number of different proposals. None to date have been adopted.

D. U. S. State and Federal Governments Fail to Resolve the Crisis.

State legislatures in the United States have introduced bills that would require terrorism coverage across all insurance Lines. The lack of any direct or re-insurance "back-stop" cover from the Federal Government has created a conflicted state response, with elected officials demanding full coverage while state administrative

officials, recognizing the current threat to carrier solvency and the lack of re-insurance, approve exclusions for the very insurance the officials demand.

For the past six months the Federal Government has faced a wide array of lobbying efforts as well as economic and moral arguments designed to persuade it to participate in the spreading of risk and allocation of loss occasioned by the threat of terrorist acts. These same pressures are at play in state legislatures and regulatory agencies. From the perspective of the business community, it is now a Hobson's choice of paying much more in premiums for limited coverage, (even if it is available), or of "going bare." United States citizens have uniformly demanded compensation and protection for the casualties of September 11th and have sought help for them from their government, their insurance/business sectors, and various charitable institutions. It is in this context that the Federal Government has been presented with many solutions, has considered some of them, but ultimately has done nothing except to enact the Federal Air Transportation Safety and Stabilization Act. (See Part II. E., below). In the face of the sobering reality of the current market impasse faced by insurers, the Federal Government response, with the notable exception of the aforesaid Act, has been a "wait and see" strategy. This response is ill advised and destined, without doubt, for a disastrous result if attacks outpace a solution to this crisis.

The current Republican Administration in the U. S. is understandably hesitant to enter into the "insurance business" on a permanent basis or to place itself in competition with the private sector. In its view, any governmental insurance solution must include litigation reform, tort reform, prohibitions on punitive damages, limitations on recovery of non-economic losses, the elimination of joint and several liability, limitations on pain and suffering awards, and changes in standards of proof. There has also been discussion of a Federal based regulatory system for terrorism coverage, tax deferred insurer catastrophe reserves, and long term Federal loans to insurers to help manage losses. All of these proposals and limitations have been openly debated, with different constituencies finding fault with different parts thereof. The

result has been no new governmental partnership with the insurance establishment to meet the risks of terrorist attacks.

E. The Federal Air Transportation Safety and System Stabilization Act Limited Airline and Certain Business and Government Liabilities.

There are several historic examples of national government insurance programs including: the Federal Housing Administration Act - which insures mortgages; the Veterans Administration - which does the same thing; and the Price-Anderson Act -which provides backup coverage for nuclear facilities. Yet, the first and only "insurance" program created to date by the U.S. Government to respond to the consequences of September 11th is the Federal Air Transportation Safety and Systems Stabilization Act. Its' stated goal is to protect America's air carriers as well as certain building owners, lessors and governmental agencies in the City of New York from massive losses arising from expected casualty suits. The Act has been amended by the Aviation and Transportation Security Act ("The Acts").

The Acts also provided $5 billion for damages suffered directly by the protected parties separate and apart from what they receive under their individual insurance programs and for reimbursement for expected increases in their insurance premiums. The Acts limited third party liability to $1.5 billion per event. Punitive damage awards are prohibited. Similar support for the insurance establishment and the rest of the business community has not been forthcoming.

III. SPECIFIC PERIL TERRORISM COVER – A PROGRAM TO BE UNDERWRITTEN BY INSURANCE ESTABLISHMENT AND GOVERNMENT PARTNERSHIPS WORLDWIDE.

A. Historic Government Covers for Catastrophic Losses Caused By Natural, Economic or Terrorist Events.

The United States Federal Government has traditionally offered "insurance" to protect against floods, create security for mortgages, safeguard nuclear

installations, and provide coverage for money deposited in banks. Within the last 20 years the Federal Government provided similar mechanisms to "bail out" Chrysler Corporation, the U. S. savings and loan industry and, most recently, under The Acts, the U. S. airline industry and certain New York City building owners, lessors and governmental agencies. The lessons learned in these efforts can be adapted to help create governmental insurance designed to "back-stop" coverage from the private sector for terrorist-caused losses in the near and far term.

Lessons can also be learned from government sponsored terrorism coverage in place in the United Kingdom, Spain, South Africa and Israel. In the United Kingdom, Pool Re provides coverage for losses no longer met by the international re-insurance market which arise out of IRA terrorism. Pool Re provides limited private coverage with additional excess coverage made available through the pool. The Government of the UK acts as a re-insurer of last result and protects the assets of the pool. In Spain, Consorclo de Compensecion de Seguros ("CCS") is a governmental insurance facility that protects against earthquakes, volcanic eruptions, floods, storms *and terrorism,* as well as civil commotion. CCS is a partnership program, combining government funds with private policies that collect premium on behalf of CCS. The South African Special Risk Insurance Association ("SASRIA") covers political risk. (See Part III. B below) In Israel the Property Tax and Compensation Fund ("PTCF") has been created to cover property losses for war and like events. Coverage for "politically motivated violence" and terrorists acts, excluded from private policies, is offered in the PTCF. There is also a catastrophe re-insurance mechanism in place in that program.

B. Traditional Political Risk Coverage Can Provide Valuable Lessons on Rating and Structuring the Program.

U.S. and other private and government insurers currently provide political risk insurance (a Property Lines cover). A $50 million political risk policy can cost anywhere from $500,000 to $2 million per year, as compared to $50,000 to $200,000 for traditional Property Lines policies insuring the property of international businesses.

Insurers have developed a premium rating system for this cover based upon what is called "country risk." The actuaries analyze corruption, political unrest, revolutionary upheaval, civil wars and other political events that may shift the balance of power in a given nation. The economic significance and the role played in a particular society by the industry to be protected are also factored into their equations. Is a potential insured a natural target for terrorist acts or is it likely to be left alone? Companies offering this coverage include Chubb, AIG and Lloyds of London. Several European governments, as well as the World Bank, offer similar protections.

Political risk insurance is limited to property losses and grants the carrier ownership of any insured property that becomes the subject of a claim. Insurers pay the claim and then recover and sell the property to reduce the loss. Such recovery is not an offset against premiums collected. This cover insures a specified peril separately under private or government programs, or in partnerships between both entities. Thus, this cover provides an example of premium rating expertise, albeit limited to first party property losses, for a profitable market driven insurer/government program. It can, therefore, serve as a model, in part, for the SPTC Program proposed here.

C. The Program's Proposed Governmental Role.

It is obvious from the magnitude of the terrorist risk, and from the limited capacity of the private insurance market in the United States and other nations to cover it, if at all, that governmental participation in some form is required. In the near and the far term, governments must address a myriad of market based and public policy questions raised by terrorist losses. The answers to these questions will shape the future of terrorism coverage. Moreover, governments alone can undertake a critical role in this Program that only they can play. The *sine qua non* of Property/Casualty insurance has always been "loss control." Simply put, insurance loss control experts "walk the plant" of an insured and finds first party and/or third party hazards which, if eliminated, serve to lower the risk of loss *and* the premium. More importantly, "Loss control" also serves to prevent needless destruction of life and property. In addition to

providing great financial resources for the Program, governments can play a critical and unique "loss control" role. Governments are uniquely suited to "walk the global plant", if you will, to try to prevent or limit acts of terrorism. Neither insurers nor insureds are as equipped as sovereign states to perform this traditional insurance function, though they, and indeed all sectors of society, must do their part.

To those that argue governments should take this risk over entirely, the response is that most of them are not prepared or equipped to handle claims or manage their defense. The insurance industry is the more capable party. Its claims handling mechanisms are in place and need not be created from whole cloth. Moreover, this mechanism is *already paid for* as part of the Property, Personal and Casualty Lines infrastructure. Moreover, private sector insurance performs an essential function in free societies. It supports, in significant part, the civil justice systems in many nations. It is insurance that pays the settlement or award that makes the plaintiff whole, (which in turn pays his lawyer), and that pays the defendant's attorney. Without insurance, most ordinary citizens would not have access to or the protections of civil justice systems.

Although the amount of the terrorist risk it can cover is finite, insurance is an efficient and essential market mechanism which collects money from and returns it to all segments of society, through investments, payment of claims and awards and the creation and jobs on a very large scale. Premiums from Personal, Property and Casualty Lines should, therefore, stay in the private sector. Only after the insurance establishment's separate terrorism loss market limits (fairly determined and uniformly set as percentages of premiums or surplus) are exceeded, should the government play a financial role. That role ought to maximize its unique infrastructure, including its powers to tax and its freedom to create liquidity to respond to these losses with cash payments on a basis that is unparalleled in the private sector. Carrier capital, private market investment capacity and claims handling expertise, paired with the financial resources of government, is the most efficient method in developed nations to continue this coverage through an SPTC Program. Partnerships of private markets and

government are the hallmark of successful historic programs that cover catastrophes clearly beyond the abilities of either player to economically, efficiently or fairly manage alone. Why should terrorism coverage, clearly required to respond to catastrophic loss, be any different?

The following basic questions must be debated and resolved in the process of creating the governmental role in the SPTC Program:

- Will such a partnership become an anti-market and/or inefficient "bailout"?
- Will government replace and thereby depress an already unstable direct and re-insurance market by limiting the amount of premium and diverting those resources away from the private sector?
- What tort and litigation reforms should initially be part of any such Program and which components of these changes should be tabled, so as to not unduly delay implementation of this important protection?
- How can treasury dollars be paid to carriers and/or claimants, without the typically exorbitant administrative fees that often attend governmental indemnity programs?
- Should there be Federal regulation of this new cover in the U. S. (or other nations) standing separate and apart from the various U. S. regulatory schemes in the 50 states, the District of Columbia and Puerto Rico?
- Will governments be the "guaranty fund" of last resort for any failed private company whose demise is traced to its terrorist caused losses?

The lessons of the not so distant past are available to shape and mold the Program's governmental role. We neither have to "reinvent the wheel", nor unnecessarily burden the Program's creation process with extraneous issues which can be addressed in the far term. Questions of state versus Federal regulation, antitrust protection, tax free surpluses, tort reform, litigation reform and the like are important

issues and they must be addressed. But these concerns do not have to be *resolved before the Program is created.* To get sidetracked now is to risk a massive failure of insurance markets, the loss of protection and the growth of fear.

D. The Program's Framework Can Serve to Spread the Risk and Allocate the Losses of Terrorism on a National and International Scale.

Historically, terrorism coverage in the United States has been a creature of "all risk" insurance policies regulated by the 52 jurisdictions. Inherent in the "all risk" underwriting concept is the proposition that everything is covered unless it is excluded. However, given the market's limited ability to provide insurance for terrorist acts and the complexity that attends forecasting loss in this arena, is it not wiser to cover specified losses under progressive "layers" of private, national and international insurance? Classic insurance programs for major risks often have primary, umbrella and excess coverage layers. That structure can serve this Program well. The Program would use the private insurance sector as a "primary layer," followed by a governmental "umbrella layer." Above that, all remaining coverage would be in an international pool of participating countries to provide a U. N. Fund "excess layer".

The United Nations is unique in its ability to gather resources to create such an "excess layer" Fund. An agency created by or under the auspices of that organization can draw from the insurance and government establishments of each sovereign worldwide to create a U. N. Fund that would be compatible with the underlying two "layers" available in each nation. The basic approach would be to rely upon cooperation among the carriers in each nation and among the participating governments, rather than attempt to make major, immediate and uniform changes in the underwriting and economic infrastructures of private and public partners.

The U. N. Fund's ultimate governance and operation would be fashioned with respect for and to be compatible with the commercial and civil justice system requirements of the participating carriers and nations, as well as the geopolitical

realities of these sovereign states. The goal would be to create an entity based on the joint cooperation and responsible participation of as may sovereign states as could be induced to "pick a side" in the fight against terrorism. International re-insurers could, if they chose, be part of this Fund on a basis similar to the insurer/governmental partnerships in the various sovereign programs. Thus, there could be a portion of the U.N. Fund that had private cover paired with a cover created by participating nations, using much the same framework, mechanisms and market safeguards as are part and parcel of the proposed underlying sovereign programs.

Lest there be any doubt, the resulting three-layer approach of private, national and international resources, however each of those layers are structured, would be designed to leave in place and independent all the necessary risk sharing decisions by government and by insurers that will serve to create and then to establish the Program.

E. Program Funding, Limits and Layer Attachment Points.

Each individual insurance company that participates at the "primary" layer should be required by law to offer a uniform policy sub-limit for this cover. The Program would be viable with limits set at no more than 10% of insurance surplus or premium collections of a participating carrier, both for purposes of one loss event and for aggregate losses per policy period. If each company participates with such set limits, per event and in the aggregate, then there is no way for it to manipulate market advantage by "scamming" the Program through an anti-competitive "laying off of extra risk" on the government layer. Likewise, a sovereign's "umbrella layer" limit could be set for one event or in the aggregate at the total surplus or the total annual premiums of all carrier participants in the Program. In the United States, that would mean a governmental fund of approximately $300 billion, if based on surplus, or $300 to $400 billion if based on annual premiums. In the alternative, a set percentage of each nation's Gross Domestic Product could serve as a sovereign limit. A nation's given

Program capacity could be share internally with its insurance establishment covering 10%, and its government covering 90% of the risk.

Premium for this cover at the "primary layer" would not be separately rated or paid. It would remain "included" in the general overall policy price. Such a policy's "all risk" limits would not, however, match its terrorism risk sub-limits. The government's treasury, not premium from any sector, would fund its "umbrella layer" obligations. Likewise, there would be no premium paid to the U.N. Fund. This layer would be funded, as needed, by participating sovereigns using a pro-rata "share" system that responds to a given loss (See the share discussion below).

While limits and pricing are areas of great debate, these solutions are proposed for several reasons. Solvency is protected by the "right" limits. Elimination of premium payments to the sovereign and to the U.N. Fund serves to keep a nation's dollars in its private economic market sectors. Once premium is transferred to a government or to the U. N. Fund, political pressures are generated that can be irresistible. Demands that such funds to be used for "other appropriate purposes" would be unrelenting. Government/U. N. collected "premiums" soon would become government/U. N. "revenue." Then monies designed to protect against catastrophic loss would begin to be used for budget deficits, entitlements, *and* the like. Such "public policy" agendas might include providing payments based on particular social or economic factors rather than the amount of the actual loss. For example, the economic circumstances of small business or low income casualties could distort loss allocations. There would also be attempts to divert these funds to rebuild public infrastructures, rather than to protect the businesses and the people who directly would be covered. Obviously, there are those who think that such use of funds from these layers is superior to a program of payments based on specified loss. The lack of any premium accumulations at the "umbrella" or "excess" layers will forestall such a debate.

Moreover, governments need not collect premium. Government reserves exist on a tax-free basis and nations have the unique ability to prevent their own insolvency. Thus, they have more immediate access to cash and more liquidity than mere premium would provide. They also have the ability to borrow, if necessary, at extremely favorable rates, access to tax free reserves built up over time, and the power to mandate coverage at set limits in the private sector to ensure that an adequate premium base is "at work" in their nation. Sovereigns in developed nations have an ability to quickly and efficiently raise and allocate huge sums of cash. No private insurance mechanism can duplicate that role.

The U. N. Fund's "dollar" attachment point would be different for each country because it would be based on that nation's individual GDP or insurance surpluses. A "payment call" on the U. N. Fund would be paid on a "share" contribution basis by participating sovereign states for a given loss. Thus, contributions for loss would be on a *case-by- case basis,* making "premiums" unnecessary. Contributions for the expenses of operating the U. N. Fund would likewise be based on each sovereign's "share" and would actually be paid annually. The U. N. Fund "share" for each sovereign could be determined by classic market forces and geopolitical realities relevant to that nation's terrorist risk. Thus, "shares" would first be based on *pro-rata* formulas using Gross Domestic Product or total insurance surplus. Next, it should not be difficult to further adjust or quantify such "shares" based on relative risk using the lessons learned in placing political risk covers over the past few years. (See Part III. B., above.)

Independently creating national programs and policy forms makes more sense than proposing the immediate creation and imposition of uniform Program components at all "layers." Endless fights over the superiority of various national justice systems or policy forms should be avoided. There need be only a clear understanding as to the specific perils insured and an acceptance of the fact that, under such an approach, neither every part of every loss flowing from an event can or will be

covered by every partner, nor will every loss be fully compensated. Losses must be covered at levels that permit financial stability for the partners at each of the three "layer." In short, coverage would be fair, but windfalls would not be in the offing.

F. A Proposed Definition for Specific Peril Terrorist Cover.

A specific peril approach requires a separate coverage grant definition. Below is a starting point for the drafting debate concerning the scope of the SPTC Program. (See Part III. H., below, for a fuller discussion of this topic.)

> "A terrorist event loss is defined by the consequences and the purpose of the act that produces it. A terrorist act has as its consequence bodily injury, death, both tangible and intangible property damage, and the interruption, disablement or destruction of business or governmental operations and/or of their infrastructures. Such losses may be intended or simply be caused by the circumstances that directly attend such an event. The purpose of a terrorist act is to influence, disrupt or eliminate a sovereign state's policies, economy, operations or infrastructures, by means of the aforementioned acts, in order to create or perpetuate fear in the minds of the citizens of the sovereign or its leaders."

The creation of the SPTC Program has three basic requirements, each of which is only possible if there is a common underwriting philosophy underlying all of the numerous forms that will make up this cover throughout a given nation and the world. These requirements are incompatible with the existing "all risk" language approach of today's covers. First, the resources of a sovereign state and its insurance establishment will have to be adapted to respond to the losses from terrorist events, without jeopardizing the ability of both partners to remain solvent. Second, the cover will have to be implemented through a Program built on, utilizing and adapting the

existing infrastructures and historical roles of these partners. Third, the specifics of the cover forms will have to be developed independently and over time, through the combined efforts of private carriers, traditional drafting entities, and the 52 regulatory agencies. Over time, classic market forces, loss experience and participant cooperation could well result in a more uniform approach to the cover. However, this process cannot begin, let alone succeed, without some common agreement to and understanding of the scope of coverage. The above coverage grant thus defines and limits the scope of the Program and its Specific Peril Terrorism Cover.

The task at hand should proceed in the context of a global examination of and response to this new threat. The United Nations should convene a conference of insurance professionals, coverage lawyers, state and national regulators and government statesmen to facilitate the creation of new Specific Peril Terrorism Cover in each nation and to coordinate these Programs so that they might participate in the U. N. Fund. The U. N. is uniquely suited to coordinate the creation of the proposed Program, with its "primary and umbrella" layers at the national level and its "excess layer" at the international level. The Program ought to be created by its participants from "the bottom up" rather than having it be instituted and imposed from "the top down." Such a conference would engender widespread participation. This, in turn, would ensure that the proposed Program would genuinely reflect, respond and apply to the true nature and scope of this threat in each nation and worldwide. Lessons learned in the United Kingdom, Spain, South Africa, Israel and the United States in creating past insurance covers for like events promise a chance for the efficient and successful creation and implementation for this new cover. (See Part III. A. above.)

G. Mandatory Coverage Would Serve to Protect Solvency and Maximize Risk Spreading.

The SPTC Program should be mandatory in all Lines. Setting the correct policy sub-limits and governmental attachment points would protect and preserve solvency. Thus, every element of society is engaged in the Program by free market

dynamics, rather than government fiat alone. Depending on how the new per event and aggregate limits are structured, a very efficient and prudent allocation of individual, business, insurance and government capital risk could be achieved.

The new terrorism cover will encompass all the classic lines of Personal, Property and Casualty insurance that generally covered terrorist losses before September 11th. The policies in these Lines would have to be adapted to provide a Specific Peril Terrorism Cover. Special premiums need not be added to the traditional general price of these covers. If all policyholders pay a market set premium to the private insurance establishment for *all covers, including this one,* then the "rule of large numbers" protects now expanded risk to be assumed by the insurance establishment on the "primary layer." The separate SPTC previously available in special markets could continue as part of the Program. Market forces will set premium in each Line to cover "all risks" and the SPTC. In this way, no one segment of society will be unfairly subsidizing another for this loss. Instead market forces and individual choice will mandate one's coverage for terrorist loss. Premiums already have, for the past year, been increasing in light of the new market realities. Premiums, although different depending on the risk and policy limits, will continue to increase generally, but there ought not be a "separate price" for this cover.

Those who chose not to purchase any line of insurance or who do not receive the benefit of the new cover through their employment, would not be protected by the proposed Program. Assuming an individual or business has the resources to enter the Program at the "primary layer", this is not an inequitable result. Thus individual choices on where to allocate resources will drive the protection. However, careful thought must be given to the critical question of how to deal with persons or business entities that have no ability to purchase the relevant Lines in the Program because of limitations in their resources or the resources of their employers. The mandatory nature of the coverage for this protection and the different resources of individuals and businesses will likely serve to focus and renew a debate long at the

forefront of U.S. life: How do we ensure an adequate safety net of health, life, property and casualty insurance for all of our citizens? Once the SPTC cover is in place, society must respond to the question of equal access to the protections of terrorism insurance. There is nothing new in this debate that is unique to the terrorism cover. This question must be answered for all insurance coverages. Thus, whatever the solution is for this general problem, it can likewise serve as the solution for SPTC. Implementation of the SPTC cannot await resolution of this important issue. It is equally true, however, that resolution of this issue ought not be delayed over long simply because, for the moment, we do not have time to resolve it.

H. Program Policy Drafting and Coverage Issues.

Under the existing U. S. infrastructure, the SPTC Program will have to be approved in each of the 52 jurisdictions that currently govern policyholder and carrier rights and obligations. The specific perils cover, based on the above or a like definition, would have to be drafted in language that was clear, concise and not susceptible to interpretation as an "all risk" policy. The SPTC in each Line would stand alone as an endorsement or as a separately defined protection in policies revised to integrate this new approach to this old cover. This approach should prevent unwarranted expansion or redefinition of the SPTC by the courts. Each company would, in the first instance, develop its own forms. However, there is no reason why there could not be cooperation and coordination in the drafting of the new provisions needed for this cover in the various Lines. Traditional drafting entities (ISO), regulatory agencies (NAIC) and insurance professionals could work together to suggest standard provisions. As noted above, ISO has performed just such a function in the U. S for over 75 years. Thus, the cover at the primary, umbrella and excess covers in the Program's "primary layer" of private insurance would not start out as uniform product. Yet over time, market pressure, loss experience and cooperation would lead to a largely uniform approach nationally and, eventually, internationally.

The underwriting decisions for the SPTC will not be global or directed in any way by governments or the U. N. These public "umbrella and excess layers" will simply sign on to the private market driven "primary layer" covers at the appropriate attachment points and fund claims beyond the capacity of a given Program "layer" for an individual loss or in the aggregate. In short, market forces in each sovereign state would help shape the underwriting of the private "primary layer" to which the public "umbrella and excess layers" would "follow form," not by providing or creating a separate policy, but by simply "back-stopping" the losses covered under the individual "primary layer" policies.

Existing specific peril underwriting principals and the lessons learned from unfounded and unwarranted coverage decisions by courts must be applied to the drafting of the new Specific Peril Terrorism Cover in all Lines. There were distortions to and the outright re-writing of underwriting intent and policy language by a few U. S. courts in the 80's and 90's that served to create coverage for asbestos, toxic tort and environmental losses where none existed. This in turn lead to the bankruptcy of far too many insurance companies that could not have foreseen, let alone prepare for, the massive losses that followed and that it never agreed to cover. All of this "drafting history" serves as a cautionary tale that must to be borne in mind when drafting the scope of coverage grant for the Program.

In light of the foregoing, care must be taken to ensure that:

- Appropriate single event and aggregate limits are created and protected at every "layer."
- Only one policy period is triggered for any one event. There is to be no "stacking" or allocating of limits over multiple policy periods; i.e., no "continuous" or "double/triple" triggers or the like.

- Multiple limits from policies triggered in one period are not "stacked" for a given loss and such "congruent" coverages do not permit double recoveries.
- Multiple losses arising from a single event are not interpreted to be multiple events, thus attaching multiple event limits which unnecessarily and prematurely exhaust coverage; *i.e.*, policy forms must specify exact periods of time which are to transpire between "events" and how these periods are to be measured.
- Private carrier insolvencies arising from these losses are remote. Thus, an appropriate and specifically designated guaranty fund should be part of every sovereign's role.
- Business interruption coverage specifically protects against physical loss or damage to tangible property, as well as to loss of gross earnings that result directly from interruption of interference with a particular business.
- Coverage for intangible property damage such as loss of suppliers, clients or customers or other disruption of commercial life is specifically defined or limited.
- Separate caps are provided for electronic equipment, furniture, business documents and data losses.
- There are clearly defined time limits in which claims can be mad; *i.e.*, policy-based statutes of limitation.
- Separate caps are in place for biological, chemical or nuclear attacks. Initially, these special sub-limits will have to be re-insured by the government and U. N. "layers" until such time as the private re-insurance market extends to this particular cover.

Consideration of specific exclusions in SPTC should include the following:

- Misrepresentations to underwriters.

- Intentional loss caused by a claimant or an insured.
- Fraud and collusion.
- Criminal acts. However, certain criminal attacks, such as those directed to abortion clinics, churches, mosques or temples, would be covered if specifically shown to have met the definition of a terrorist act.
- Losses flowing from governmental "credible threat warnings." There are significant problems with proofs of damage flowing from "credible threats." For example, how many credible threats constitute one occurrence or are they all separate events? How do you compensate for "preparation expenses" arising from threat "defense?" This is an area ripe for abuse.
- The full cost of replaced property; *i.e.*, there need to be set-offs based upon residual or already amortized property values as of the time of the loss.

Policy drafters always have to be careful about the language they choose. Because policies are read as a whole, the safest way to establish an SPTC is to provide it as a separate protection section in the policy or by endorsement. Care must be taken to ensure that the *other coverage grants* in each policy in each Line do not create ambiguities or contradictions for the SPTC Program.

The proposed Program should not extend to punitive, bad faith, treble, exemplary or other like damages ("punitive awards"), all of which are now available to claimants in suits against policyholders or to policyholders in suits against their carriers for "bad faith" conduct or the like. The losses covered under this Program will be extensive enough not to burden it with punitive awards. U. S. courts have been incredibly unsuccessful in bringing rhyme or reason to the imposition of punitive awards. To the extent that punitive awards are made to claimants as against an alleged tortfeasor, public policy ought to bar their coverage by insurance. These damages flow only from wanton and willful, if not intentional, disregard for life and property. The

proven case and award would stand against the insured, but would not be paid by the Program. Why protect and thus encourage that conduct with insurance?

With regard to a policyholder's like claims as against an insurance company, the government or the U. N. Fund for "failure to pay a claim" or "claims handling or coverage litigation misconduct," we suggest that Program punitive awards be limited to *set rational amounts* available only for *specified conduct.* Such conduct should be listed only in the Program policy, as approved by the national government that funds the cover. Neither courts nor other regulatory agencies ought to be permitted to add to that list. The Program's guidelines for such a list would permit punitive awards only for *specific acts* of fraud or deceit and not extend them to negligence or inadvertence. In addition, provision would be made now for an award of attorney fees and costs incurred by an insured that prevails in a coverage dispute. The list could also *eventually include any specific act* that actually prejudices a person's rights, as opposed to offending their subjective expectations or feelings (see immediately below). The losses expected in a terrorist event are on such a scale that there simply is not enough money to provide punitive award "windfalls." Punitive award availability for coverage claims handling and litigation conduct, beyond the scope of the aforesaid protections, serves only to distort and unfairly cripple meritorious insurance defense strategies or to hamper or outright inhibit a carrier's rightful assertion of meritorious positions on legal issues or factual questions. These damages, unless rationally limited, serve mainly to create an unfair litigation advantage in favor of a policyholder's advocate, rather than to "protect" an aggrieved policyholder or to "prevent" future abuse.

There is a vociferous debate in the U. S. as to the role and limits of punitive awards and certain types of general damages. As that controversy plays out and is resolved, there simply should be no coverage for the punitive awards in *this* Program beyond the two categories noted above. When a solution to the general problem of excessive damage and punitive awards is achieved, it can be applied to the

Program, as and if warranted. As with the current debates on other tort and litigation reforms, the creation of the Program ought not be sidetracked by a demand for the immediate solution of all these problems.

I. Handling Program Claims.

Under this Program, the individual carriers in each nation will handle the claims under their single event loss or aggregate limits. Once either of those limits is reached, that carrier will continue to handle a given claim and simply be reimbursed by the government (or advanced funds by it to cover the loss). Thus the government "umbrella layer" of the Program performs an indemnity function, not a defense or claims management function, and will not bear the costs of making payment decisions or processing claims. Likewise, once an individual sovereign's limits are tapped (say $300 billion for the United States) the U. N. Fund 's "excess layer" will simply reimburse the carrier (or front the money for it) on a given claim. U. N. payments will be raised on an as needed basis according to the shares agreed to by the participating nations as outlined above. One would hope that under this approach, the "U. N. contribution" disputes that we have been in play over the decades would not re-occur.

J. Dispute Resolution Options.

A choice will have to be made whether third party claim litigation and all policy coverage disputes will be heard in state courts, federal/national courts and/or alternative dispute resolution "ADR" forums. We suggest only the latter two forums. We prefer the ADR approach so that an efficient and specialized mediation and arbitration mechanism could operate at the primary, umbrella and excess layers of the Program. National (*i.e.,* federal in the U.S.) court jurisdiction would serve a similar function. Resorting to the courts in the 52 U. S. jurisdictions, for example, simply does not bode well for the consistent interpretation of what is, in great part, a federal government cover. There are national and international ADR mechanisms and forums existing in each nation and on a worldwide level that have proven to be fair, consistent

and economical. The jurisdiction and processes of a sovereign's federal/national public courts, or of a worldwide court for U. N. Fund disputes, could be an alternative choice reserved for specific issues or losses of great magnitude. This solution for dispute resolution is supported by all the reasons that traditionally favor ADRs over courts. The Program could thus preserve the choice for either the national court or an ADR.

It would be essential however to include the traditional protections of the civil justice system in any ADR mechanism. These safeguards would include the following aspects of the Rule of Law: (1) formal traditional evidence and procedural rules and standards; (2) formal discovery; (3) written findings based on the applicable law; and (4) rights of appeal available to the public litigants in a given nation. Appeals could likewise proceed before public courts or special appellate ADR panels with all of the safeguards of the foregoing forums. All ADR forums would be open to the public.

The SPTC Program ought to be governed by national law, rather than state-by-state or providence-by-providence. Excepted from this exclusive jurisdiction structure would be all existing regulatory functions applicable to policy forms and other aspects of the cover that need not initially be uniform. These agencies are already in place in the 52 U. S. jurisdictions, or in like agencies in other nations, and need not be duplicated in the absence of a conflict with the national operation of the Program. Uniform federal/national administration and enforcement of the legal foundation for the Program need not replace those infrastructures. However, a body of *federal law* would be developed to replace the 52 different versions of coverage law existing now in the various states, the District of Columbia and Puerto Rico. Evidentiary and procedural rules from the same system would apply. Existing international law could be utilized to handle disputes over the U. N. Fund, all as is determined by the participating nations. Such a uniform approach would avoid forum shopping and the dislocations of contrary results flowing from competing and conflicting "state forum" coverage determinations. Program protection could thus be fair and uniform, rather than determined on the location of the tribunal within a given nation. All of the

forgoing would be applicable to ADR forums to be used under the Program. The various 52 U. S. administrative regulatory structures would be coordinated, as appropriate, with "jurisdiction" issues resolved consistent with the above suggested split of oversight and control.

IV. CONCLUSION.

The insurance carriers in the various nations of the world have limited resources and cannot be called upon to bear an unrealistic or destructive share of a given terrorist loss event or the aggregate thereof. The sovereign governments in each nation can bear a greater risk than can the private sector and are equipped to share it on a broader basis. They can also provide re-insurance until that private sector cover can be stabilized and re-enters the market. Sovereigns can thereafter mandate SPTC in all Lines and thus spread losses more evenly below national and international attachment points. Private carriers can thereby broaden the base of premium payments and help stimulate the economic and tax revenues that ultimately fund the next two "layers." Each sovereign can provide stability and security while national and international market forces adjust forms, illuminate underwriting choices and fix limits and attachment points. More importantly, as the Program matures, the insurance establishment can replenish and protect its surplus and premium base.

The role of the sovereign can, over time, be reduced or changed for some Lines in the Program or increased for others. Attachment points and limits can alter in different programs and sovereigns can reallocate their resources as market conditions dictate. All of this should serve to keep pace with the evolving threats of terrorism. Moreover, national market place responses and geopolitical mechanisms can efficiently work together to disclose the true roles being played by sovereign states in the war on terror. It simply won't be politically feasible for a nation to long both foster and be called upon to pay for terrorist acts. This realty will be one of the major benefits of a Program that, at its core seeks, to combat fear and build a sense of protection and security in the world as well as in individual nations.

ACKNOWLEDGEMENTS

The analysis, opinions, suggestions and proposals in this paper are the sole responsibility of the author and no one else. It is, however, important to note that other members of this Panel at the Conference -- **" Is There and Will There be Insurance Coverage for the Risk of International Terrorism?" --** were very helpful by commenting upon and critiquing this paper. They include: Ronald M. Greenberg, Of Counsel, Berkes Crane Robinson & Seal; Renny W. Hodgskin, Senior Vice President, Cambridge Integrated Services Group, Inc.; David R. Robb, Executive Vice President, The Hartford; and James L. Seal, Founding Partner, Berkes Crane Robinson & Seal, LLP. The comments provided by Ms. Beverly Eckert, Co-Chairperson of the Voices of September 11, a family Advocacy Group, were quite insightful and much appreciated. Additional resources came from the proceedings of the Subcommittee on Oversight and Investigation, Committee on Financial Services, House of Representatives, United States Congress and in particular, from the statement to the Sub-committee by Richard J. Hillman, Director of Financial Markets and Community Investments, General Accounting Office of the United States. Also helpful were the observations and analysis of Ellen Seidman, Senior Counsel, Democratic Staff, to the Committee on Financial Services, in her remarks to the 2002 World Insurance Forum in Bermuda and the recent Swiss Re Focus Report -- *"Terrorism – Dealing With The New Spector."* Thank you all very much.